IN THE UNITED STATES BANKRUPTCY COURT
FOR THE EASTERN DISTRICT OF TENNESSEE

In re	
KEYSTONE FARMS LP,	No. 00-22568
	Chapter 7
Debtor.	[affirmed E.D. Tenn. No. 2:02-CV-53; 04-03-2002]

M E M O R A N D U M

APPEARANCES:

J. Gregory Bowman, Esq.
Rogers, Laughlin, Nunnally, Hood & Crum
100 South Main Street
Greeneville, Tennessee 37744
Attorneys for KeyBank National Association

Kenneth J. Catanzarite, Esq.
Catanzarite Law Corporation
2331 W. Lincoln Avenue
Anaheim, California 92801

-and-

Michael Hickie, Esq.
Carrier & Hickie
206 Princeton Road, Suite 44
Johnson City, Tennessee 37601
Attorneys for William and Janet Kincaid

Marcia Phillips Parsons
United States Bankruptcy Judge

This chapter 7 case came before the court for hearing on December 4, 2001, upon a motion for relief from stay or for abandonment by KeyBank National Association ("KeyBank") and the objection thereto by William and Janet Kincaid (the "Kincaids"), unsecured creditors and equity security holders of the debtor. At the hearing, the chapter 7 trustee stated that she had no objection to the motion and after considering arguments by counsel, the court announced that KeyBank's motion would be granted. Upon entry of an order, the Kincaids appealed this court's decision to the district court.

Subsequently, on January 8, 2002, two other motions filed by the Kincaids came before the court for hearing, both of which were objected to by KeyBank: a motion to stay pending appeal the order granting KeyBank's motion and a motion requesting that this bankruptcy case be reconverted to chapter 11. Again, after hearing from counsel for the parties and the chapter 7 trustee, the court denied the Kincaids' motion to convert and took under advisement their motion for stay pending appeal. For the reasons set forth below, the motion for stay will be denied. In light of the existing appeal by the Kincaids of the order granting KeyBank's motion, and the expected appeal by the Kincaids of the orders denying their motions to convert and for stay pending appeal, the court submits the following findings of

fact and conclusions of law in accordance with Fed. R. Bankr. P. 7052. These are core proceedings. *See* 28 U.S.C. § 157(b)(A),(G) and (O).

I.

The debtor filed its petition commencing this case under chapter 11 on September 25, 2000. The sole real property listed by the debtor in its schedules was a 90-unit apartment complex located in Nashville, Tennessee known as Keystone Farms which had been scheduled for foreclosure by the Department of Housing and Urban Development ("HUD"). On June 15, 2001, HUD filed a motion for relief from stay to permit foreclosure. In response, the Kincaids filed on July 2, 2001, a memorandum in opposition to the motion, in which they stated an intention to "file a plan and disclosure statement by July 16" because they were "extremely interested in preserving and protecting their general unsecured and equity security holder interests." The Kincaids argued that the Keystone Farms apartment complex was "essential for an effective reorganization *that is in prospect*, and will be consummated within a reasonable time." [Emphasis in original.] Nonetheless, despite this initial opposition, counsel for the Kincaids subsequently executed an agreed order granting HUD permission to foreclose, which order was entered by the court on

July 31, 2001. Thereafter, the debtor voluntarily converted its case to chapter 7 on August 30, 2001.

On November 14, 2001, KeyBank filed its motion for relief from stay or for abandonment to allow foreclosure upon certain storage warehouses owned by Storage Kentucky, LLC ("Storage KY") and Storage Florida, L.P. ("Storage FL"). KeyBank stated in the motion that although the debtor "had no interest in the property at issue," the motion was filed "out an abundance of caution" because the Kincaids had filed on behalf of the debtor certain notices of lien *lis pendens* against the warehouses. Attached to the notices were copies of a complaint initiating an adversary proceeding which the Kincaids had filed in this court on July 2, 2001, on behalf of the debtor.[1]

This adversary proceeding provided the basis for the Kincaids' opposition to KeyBank's motion for relief from the automatic stay or abandonment. The defendants in the adversary proceeding are the record owners of the storage warehouses, Storage KY and Storage FL, along with the debtor's general partner, The Realty Shop, Inc. ("Realty Shop"); the president of debtor's general partner, Edward H. Street; Main Street Realty,

[1]There is no indication that the Kincaids sought permission from either the debtor or this court before filing either the adversary proceeding or the lien notices on behalf of the debtor.

LLC ("Main Street"); and Derby Self Storage, LLC ("Derby"). The Kincaids assert in the complaint that Mr. Street "used and uses the assets of the Debtor and CO-DEFENDANTS for his personal use and benefit, and so completely controlled, dominated, managed and operated the Debtor and the CO-DEFENDANTS ... that any separateness between STREET, the Debtor and the CO-DEFENDANTS have ceased to exist." The Kincaids allege, *inter alia*, that Mr. Street caused the debtor to loan approximately $250,000 to Realty Shop and $40,000 to Main Street, that Realty Shop and Main Street served as a conduit to Storage KY and Storage FL, and that in turn, Storage KY and Storage FL utilized these monies to purchase and/or improve certain storage warehouses. The Kincaids contend that as a result of these transactions, the storage warehouses are property of the debtor's bankruptcy estate. The Kincaids request on behalf of the debtor that the court order the turnover of these warehouses pursuant to 11 U.S.C. § 542 or in the alternative, the return of the loaned monies.[2]

Because of this pending adversary proceeding, the Kincaids

[2]The Kincaids also seek recovery from Mr. Street for "a minimum of $12,000" which he allegedly received "in violation of the Cash Collateral Order" with HUD. In addition, the complaint sets forth an indemnity claim against Mr. Street and Realty Shop to the extent the debtor is found liable to HUD in ongoing litigation regarding alleged violations of a regulatory agreement for the apartment complex.

asserted that KeyBank's motion for relief from stay and for abandonment of these warehouses should be denied because they constitute property of the estate which is needed for an effective reorganization of the debtor. KeyBank denied that the warehouses were properties of the debtor's estate, observing that the warehouses are owned by Storage KY and Storage FL rather than the debtor, that these entities are not in bankruptcy, and the debtor is not a member, partner, shareholder, or owner in or of these entities. Alternatively, KeyBank contended that even if the warehouses were property of the estate, there was no equity in the properties and they were not necessary for an effective reorganization. In support of the lack of equity allegation, KeyBank submitted the affidavit of Dale Clayton, a vice-president with KeyBank, who stated that as of November 6, 2001, Storage KY owed KeyBank over $2.4 million, which was secured by property appraised at $1.775 million, and that no payment had been made on the debt since January 1, 2001. With respect to Storage FL, Mr. Clayton stated KeyBank was owed over $2.5 million, which debt was secured by property appraised at $1.828 million, and that no payment had been made on the debt since February 5, 2001.

Neither the chapter 7 trustee nor the Kincaids disputed the lack of equity in the properties. Furthermore, the chapter 7

trustee stated that she was of the opinion that even if the warehouses were property of the bankruptcy estate, they were of no benefit to the estate because KeyBank holds a first, unavoidable lien on the warehouses.

After a consideration of these facts, this court concluded that the properties owned by Storage KY and Storage FL did not constitute property of the estate and therefore KeyBank was not precluded by the automatic stay from going forward with its foreclosures. First of all, it did not appear that the alter ego claim brought by the Kincaids in the adversary proceeding was property of the estate, much less the assets owned by the defendants in that proceeding. The Sixth Circuit Court of Appeals has counseled that "[w]hether a particular cause of action is available to the debtor, and thus constitutes 'property of the estate' is determined by state law." *Spartan Tube and Steel, Inc. v. Himmelspach (In re RCS Engineered Products Co.)*, 102 F.3d 223, 225 (6th Cir. 1996).

Although the Kincaids cite *Steyer-Daimler-Puch of America Corp. v. Pappas*, 852 F.2d 132, 136 (4th Cir. 1988), as authority for the proposition that an alter ego claim is property of the estate, *Pappas* was based on Virginia law, not Tennessee law. This court has been unable to locate any reported decision which addresses Tennessee law on this issue. In the *RCS Engineered*

Products decision decided by the Sixth Circuit, the court held that under Michigan law an alter ego claim is not property of the estate which may be brought by the corporate debtor's bankruptcy trustee. The court reasoned that the claim was not a cause of action which belonged to the corporate debtor prior to bankruptcy because under Michigan law, a corporation can not pierce its own corporate veil in order to pursue an alter ego theory against its shareholders or parent company. *In re RCS Engineered Products, Co.* at 226-27. Similarly, in *Ellenberg v. Waliagha (In re Mattress N More, Inc.)*, 231 B.R. 104 (Bankr. N.D. Ga. 1998), Bankruptcy Judge Bihary reached the same conclusion regarding Georgia law. As stated by the court therein:

> Defendants are correct that no Georgia court has ever addressed whether an alter ego claim may be brought by the corporation itself. It does appear that all the Georgia alter ego cases involve claims asserted by creditors. This makes sense, since the doctrine is largely a debt collection device. After reviewing the principles of corporate jurisprudence and dozens of Georgia cases involving veil-piercing claims, the Court concludes that the Supreme Court of Georgia would probably not allow a corporation to assert a claim to pierce its own corporate veil. There is something anomalous about a corporation, which is created to protect its shareholders from the liability of the enterprise, asserting a claim to destroy the very protection for which it was created. Furthermore, it is relatively difficult to pierce the corporate veil in Georgia. [Citation omitted.] The trustee unquestionably has standing to sue these defendants for any improper transfers from the debtor, and to sue

> any officer, shareholder or director for breach of fiduciary duties and negligent management. [Citation omitted.] However, the Court is not persuaded that a trustee can destroy the corporate fiction to make shareholders and related entities liable for all the debtor's debts and the trustee's administrative expenses.

Id. at 109.

Clearly, the states disagree on this issue. Judge Bihary noted that "the Second, Fourth, Fifth, and Seventh Circuits have all found that general alter ego claims become property of the bankruptcy estate and may be pursued by the trustee." *Id.* at 107. In the *RCS Engineered Products* case, the Sixth Circuit observed that in an Eighth Circuit decision, the court had concluded that under Arkansas law, a trustee did not have standing to assert an alter ego claim, *see In the RCS Engineered Products Co.*, 102 F.3d at 225 (citing *In re Ozark Restaurant Equipment Co.*, 816 F.2d 1222 (8th Cir. 1987); while a bankruptcy court in Ohio reached a contrary conclusion with respect to Ohio law. *Id.* (citing *In re Lee Way Holding Co.*, 105 B.R. 404 (Bankr. S.D. Ohio 1989)).

Like the Georgia cases, all of the Tennessee cases have involved efforts by creditors to pierce the corporate veil; none involved a corporation which sought to disregard its own corporate form. And, as in Georgia, the separate identity of a corporation is not easily disregarded in Tennessee. "The

principle of piercing the corporate veil is to be applied with great caution and not precipitately, since there is a presumption of corporate regularity." *Muroll Gesellschaft v. Tennessee Tape, Inc.*, 908 S.W.2d 211, 213 (Tenn. App. 1995). Furthermore, the language utilized by the Tennessee courts is similar to Michigan law on the subject as addressed by the Sixth Circuit in the *RCS Engineered Products* decision. *Compare In the RCS Engineered Products Co.*, 102 F.3d at 226 ("corporate veils will be pierced only to prevent fraud or injustice"), *with Muroll Gesellschaft*, 908 S.W.2d at 213 ("The separate identity of a corporation may be disregarded upon a showing that it is a sham, or dummy or where necessary to accomplish justice."). Based on the foregoing, this court concludes that because under Tennessee law a corporation would not be allowed to pierce its own corporate veil, the alter ego claim asserted by the Kincaids is not property of the debtor's bankruptcy case.

Secondly, even if the alter ego claim asserted by the Kincaids against the defendants in the adversary proceeding constituted property of the estate, this court was not convinced that this fact transformed assets of the defendants, such as the storage warehouses owned by Storage KY and Storage FL, into property of this debtor's estate. The alter ego claim has not been litigated and presumably Storage KY and Storage FL have

their own creditors who will seek to assert an interest in their assets. Furthermore, the court was concerned about the attenuated nature of Kincaids' claim against Storage FL and Storage KY. The Kincaids were not asserting that the debtor loaned monies to these entities which money should be returned. Instead, the Kincaids asserted that the debtor loaned monies to the Realty Shop and Main Street and that these entities then conveyed the loaned monies to Storage FL and Storage KY, who then utilized the funds to purchase the warehouses, and that therefore these warehouses are property of the debtor's estate. This court did not accept this proposition and noted that the Kincaids were unable to cite any reported decision where under similar facts the assets of Storage KY and Storage FL were property of the bankruptcy estate.

This court's decision granting KeyBank's motion was also based on the conclusion that even assuming the warehouses were property of the debtor's estate, KeyBank was entitled to automatic stay relief. 11 U.S.C. § 362 (d)(2) provides that "with respect to a stay of an act against property," relief from the automatic stay may be granted if "the debtor does not have any equity in such property" and "such property is not necessary to an effective reorganization." While the Kincaids did not dispute the lack of equity in the Storage KY and Storage FL

properties, they nonetheless argued that the properties were necessary to an effective reorganization. Under 11 U.S.C. § 362(g)(2), the Kincaids bore the burden of proof on this issue. "What this requires is not merely a showing that if there is conceivably to be an effective reorganization, this property will be needed for it; but that the property is essential for an effective reorganization *that is in prospect*." *United Sav. Ass'n of Texas v. Timbers of Inwood Forest Assoc., Ltd.*, 484 U.S. 365, 375-76 (1988) (emphasis in original). In other words, "there must be a reasonable possibility of a successful reorganization within a reasonable time." *Id.* at 376.

In this regard, the court noted that this case was filed as a chapter 11 by the debtor in September 2000 and the exclusivity period for the debtor expired in January 2001. After that date, the Kincaids could have proposed a plan of reorganization for the debtor. *See* 11 U.S.C. § 1121(c). Yet none was filed. On July 2, 2001, the Kincaids filed the adversary proceeding which they now assert provides the basis for a reorganization by the debtor. Presumably by that time, the Kincaids possessed all the facts necessary to propose a plan based on the relief sought in the adversary proceeding. Yet no plan was filed. Also, on July 2, 2001, the Kincaids filed an objection to HUD's stay relief motion in which the Kincaids represented that they would

"file a plan and disclosure statement by July 16." Not only did the Kincaids not file a plan as promised, they did not object when the debtor voluntarily converted this bankruptcy case from chapter 11 to chapter 7 on August 30, 2001, even though their adversary proceeding was already pending at the time.

At the hearing on December 4, 2001, when this court considered KeyBank's stay relief motion, more than five months had passed since the Kincaids' adversary proceeding was filed. Furthermore, more than three months had elapsed since this case was converted to chapter 7. Yet despite this time passage, despite the Kincaids' numerous opportunities to file a plan and its failure to do so, and despite the Kincaids' failure to object to chapter 7 conversion even though its adversary proceeding was pending, the Kincaids argued in opposition to KeyBank's motion that the Storage KY and Storage FL properties "[were] essential for an effective reorganization **that is in prospect**, and will be consummated within a reasonable time." [Emphasis in original]. However, clearly no reorganization is in prospect. No plan has been filed and even if it were, it would be dependent on the successful completion of an adversary proceeding which the Kincaids have been slow to prosecute. Although the Kincaids completed service of process on August 28,

2001, no answer or other response to the complaint has been filed and the Kincaids have not moved for default judgment.

When faced with a motion for relief after the exclusivity period has expired, a plan proponent generally must demonstrate that a successful reorganization within a reasonable time is "assured." *See In re Holly&s, Inc.*, 140 B.R. 643 (Bankr. W.D. Mich. 1992). Because the Kincaids failed to demonstrate that successful reorganization within a reasonable time was "assured," or even reasonably possible, relief in favor of KeyBank was appropriate. In light of the foregoing, the court authorized the chapter 7 trustee to sign the necessary documents to release the liens *lis pendens* and otherwise remove the cloud on title placed on the properties by the Kincaids.

II.

On December 24, 2001, the Kincaids filed an appeal of the order granting KeyBank's motion along with a motion to stay enforcement of that order. KeyBank filed an objection to the motion to stay on January 8, 2002. A motion for stay of judgment or other order pending appeal under Fed. R. Bankr. P. 8005 is discretionary. *See First Nat'l Bank of Boston v. Overmyer (In re Overmyer)*, 53 B.R. 952, 955 (Bankr. S.D.N.Y. 1985). The criteria to be evaluated under Rule 8005 are as

follows: (1) the likelihood that the party seeking stay will prevail on the merits of the appeal; (2) the likelihood that the movant will suffer irreparable injury unless the stay is granted; (3) whether other parties will suffer no substantial harm if the stay is granted; and (4) whether the public interest will be served by granting the stay. *See Stephenson v. Rickles Electronics & Satellites (In re Best Reception Systems, Inc.)*, 219 B.R. 988, 992 (Bankr. E.D. Tenn. 1998)(discussing *Michigan Coalition of Radioactive Material Users, Inc. v. Griepentrog*, 945 F.2d 150, 153 (6th Cir. 1991) and *Bradford v. J.C. Bradford & Co. (In re Bradford),* 192 B.R. 914, 917 (E.D. Tenn. 1996)). Although the four factors are "integrated considerations that must be balanced together," the "movant is always required to demonstrate more than the mere 'possibility' of success on the merits" and "is still required to show, at a minimum, 'serious questions going to the merits.'" *Griepentrog*, 945 F.2d at 153-54.

In this instance, the Kincaids have failed to show "serious questions going to the merits" of this court's decision granting KeyBank's motion. Based on this court's analysis of the law, it is highly unlikely that an appellate court will conclude that the storage warehouses are property of the debtor's estate. More importantly, the Kincaids neither disputed the validity of

KeyBank's secured position in the Storage KY and Storage FL properties nor did they claim that KeyBank's first priority position would somehow be diminished if those properties were brought into the debtor's estate. Therefore, as this court observed, even if the properties were considered to be property of the debtor's estate, KeyBank was entitled to relief from the automatic stay because there was no equity in the property and the Kincaids failed to demonstrate that a successful reorganization within a reasonable time is assured. Upon an appeal, this court's factual determination is reviewed under the clearly erroneous standard. *See Nicholson v. Isaacman (In re Isaacman)*, 26 F.3d 629, 630 (6th Cir. 1994).

The Kincaids state that they will suffer irreparable harm if a stay is not granted because the properties "will no longer be available to reorganize" and "no adequate remedy will be available to the Kincaids and to other unsecured creditors because the amount of damages cannot be easily calculated." On the other hand, the Kincaids argue that KeyBank will not suffer any harm if a stay is granted because the Kincaids propose to post a supersedeas bond in the amount of $18,021 per month to protect KeyBank's interest pending appeal. This bond amount is based on a 6% annual return on the values placed on the warehouses by KeyBank's expert.

As to the Kincaids' first contention, the Kincaids are correct in their assessment that their appeal is rendered moot if KeyBank is allowed to move forward with its foreclosure of the warehouses. See *Egbert Dev. LLC v. Community First Nat'l Bank (In re Egbert Dev. LLC*), 219 B.R. 903 (B.A.P. 10th Cir. 1998), and cases cited therein. This factor, however, is offset by the unlikelihood that reversal on appeal will occur. Furthermore, it should be noted that in the Kincaids' adversary proceeding, they requested that either the warehouse properties be turned over to the debtor's bankruptcy estate "or, alternatively, that monies received by said CO-DEFENDANTS be returned to the estate." By making this alternative prayer, the Kincaids have in effect conceded that an adequate remedy at law exists in the form of a monetary judgment for the monies which Mr. Street allegedly caused the debtor to advance. The Kincaids will still be able to pursue a monetary judgment against the defendants in the adversary proceeding even if KeyBank forecloses the properties at issue.

With respect to the potential harm which a stay would impose on KeyBank, the creditor denies that the bond which the Kincaids propose to post is in an amount sufficient to prevent harm to KeyBank. In support of this proposition, KeyBank has tendered the affidavit of Dale Clayton wherein Mr. Clayton states that

KeyBank has obtained an offer for the Storage KY property from a third-party purchaser in the amount of $2.2 million and that this sale will not take place if it is delayed pending an appeal of this court's decision. Due to the potential loss of this purchaser, KeyBank contends that the only way it can be adequately protected during an appeal is if the Kincaids post a full cash bond in the amount of the purchase price with respect to the Kentucky property and provide adequate protection with regard to the Florida real property. The court agrees and finds that the Kincaids& proposed bond is inadequate to protect KeyBank from suffering substantial harm if its order is stayed while the Kincaids pursue their appeal. As for whether the public interest would be served by a stay, the Kincaids assert that "a stay would prevent KeyBank from selling the real properties to third parties," and therefore "[a] stay would serve the public interest by protecting innocent, bona fide purchasers in the real properties from unnecessarily suffering protracted litigation if a reversal is granted." However, this argument assumes that a reversal on appeal would affect a sale by KeyBank. The law is to the contrary. *See In re Egbert Development*, 219 B.R. at 905. Furthermore, a reversal would not affect KeyBank's first priority position or change the fact that KeyBank is undersecured on two obligations for which it has not

received any payment in a year. To require a secured creditor to lose a prospective purchaser and await the conclusion of an appeal which has only a remote chance of succeeding is in this court's view an affront to the public's interest. For all of the reasons discussed above, the Kincaids' motion for stay pending appeal will be denied.

III.

Finally, the court turns to the motion to convert this case back to chapter 11 filed by the Kincaids on November 30, 2001, and the objection thereto filed by KeyBank on January 8, 2002. The basis for the Kincaids' conversion request was so they could propose a plan of reorganization concerning the properties owned by Storage KY and Storage FL and so that a chapter 11 trustee could be appointed to investigate the matters raised in the Kincaids' complaint. However, KeyBank has been granted permission to foreclose upon the Storage KY and Storage FL properties and a chapter 7 trustee has already begun such an investigation. Furthermore, as noted with respect this court's ruling on KeyBank's stay relief motion, the Kincaids could have proposed a plan of reorganization and/or filed a motion requesting the appointment of a trustee while this bankruptcy case was still in chapter 11 but inexplicably failed to do so.

The court sees no reason to give the Kincaids "a second bite at the apple" when they never took the first bite available to them. These factors, along with the absence of any real prospects for reorganization within a reasonable period of time, lead this court to conclude that cause for reconversion had not been established.

IV.

In accordance with the foregoing, an order will be entered contemporaneously with the filing of this memorandum opinion denying the Kincaids' motion for stay pending appeal.

FILED:

BY THE COURT

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MARCIA PHILLIPS PARSONS
UNITED STATES BANKRUPTCY JUDGE